



HIGH PLAINS ENERGY INC.

ANNUAL YEAR-END FINANCIALS

For the Year Ended December 31, 2004

And Corresponding

MANAGEMENT'S DISCUSSION & ANALYSIS

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and analysis dated April 29, 2005 is provided by the management of High Plains Energy Inc. ("High Plains") in accordance with Canadian generally accepted accounting principles ("GAAP") and should be read in conjunction with the audited consolidated financial statements and notes thereto for the years ended December 31, 2003 and December 31, 2004.

Management's Discussion & Analysis (MD&A) is intended to assist in the understanding of the trends and significant changes in the financial condition and results of operations for the year ended December 31, 2004.

Additional information relating to High Plains is available on SEDAR at www.sedar.com.

Non-GAAP Disclosure

The MD&A contains the term cash flow from operations which should not be considered an alternative to, or more meaningful than, net income as determined in accordance with GAAP as an indicator of High Plains' performance. High Plains' determination of cash flow from operations may not be comparable to that reported by other companies, but is a financial term commonly used in the oil and gas industry. The reconciliation between net income and cash flow from operations can be found in the Consolidated Statements of Cash Flows.

Common Unit of Volume

Where amounts are expressed on a barrel of oil equivalent basis (Boe) natural gas volumes have been converted to a common unit of measure on the basis of six thousand cubic feet (Mcf) of gas to one barrel (Bbl) of oil. Boe figures may be misleading, particularly if used in isolation. Volumes of gas production are reported on the basis of sales gas volumes.

Foreign Exchange

Monetary assets and liabilities of integrated foreign operations are translated into Canadian dollars at the rate of exchange in effect at the balance sheet date. Other assets, liabilities, and items affecting earnings are translated into Canadian dollars at rates of exchange in effect at the date of the transaction, except for depletion, amortization and accretion. Depletion, amortization and accretion are translated at the same rate as the related assets. Gains or losses arising from foreign currency translation are included in the determination of income.

Forward-Looking Statements

Certain information regarding management's assessment of High Plains' future plans and operations that are not historical facts may be considered "forward-looking statements". Since forward-looking statements address future events and conditions, by their very nature they involve inherent risks and uncertainties. Actual results could differ materially from those currently anticipated due to any number of factors, including such variables as new information regarding recoverable reserves, changes in demand for, and commodity prices of crude oil and natural gas, legislative, environmental and other regulatory or political changes, competition in areas where the Corporation operates and other factors discussed in this interim report.

Use of Estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The amounts recorded for depletion and depreciation of property and equipment and the provision for asset retirement obligations and the ceiling test are based on estimates of gross proven reserves, production rates, oil and gas prices, future costs and other relevant assumptions. These estimates are reviewed regularly and changes in such estimated in future years, could be significant. As adjustments become necessary, they are reported in earnings in the periods in which they become known.

Changes in Accounting Policies

Asset Retirement Obligation

In the first quarter of 2004 the Company retroactively adopted the recommendations of the Canadian Institute of Chartered Accountants on accounting for asset retirement obligations. The new pronouncement requires recognition of the fair value of the liability for an asset retirement obligation in the period in which it is incurred and a corresponding increase in the carrying value of the related asset. This change in accounting policy is described in note 3 to the consolidated financial statements. Adoption of this standard increased the Company's asset retirement liability by \$410 thousand and increased property and equipment by \$400 thousand, the difference being the effect of the related depletion.

Operational and Financial

Net income of \$281 thousand (\$0.05 per share) for the year ended December 31, 2004 was down from \$323 thousand (\$0.06 per share) for the year ended December 31, 2003. Increased administrative expenses, partially offset by a future tax recovery accounted for the decrease. Cash flow from operations was \$473 thousand (\$0.08 per share) for the year ended December 31, 2004, a decrease of 28% from \$661 thousand in 2003.

Petroleum and Natural Gas Revenues

Revenues from oil and gas sales were \$1.7 million in the year ended December 31, 2004 compared to \$1.8 million in the same period in 2003. Revenues were lower in 2004 primarily as a result of an 8% decrease in natural gas wellhead price attributable to the renegotiated price for gas produced in Montana, and the suspension of approximately 7 barrels per day of crude oil production in the third quarter to safely accommodate the drilling of a new well. For the year, gas sales volumes remained steady at 533 Mcf per day, while crude oil and natural gas liquids production increased by 4% to 21 barrels per day as a result of higher natural gas liquids sales from the Chedderville property.

Corporate crude oil, NGL and natural gas sales were 110 Boe per day for the year 2004 compared to 109 Boe per day for the same period in 2003. Natural gas comprises approximately 80% of the production. The average 2004 wellhead price was \$42.22 per Boe, down 4% from \$ 44.06 per Boe in 2003, mainly due to the reduced Montana gas price.

Royalties

Royalty expenses were \$246 thousand, or 14% of petroleum and natural gas revenue in the year ended December 31, 2004 compared to \$229 thousand or 13% of revenue during the same period in 2003. The increase in royalties resulted from greater sales in Alberta where royalty rates are higher. On a unit of production basis, royalty expenses were \$6.11 for the year 2004 compared to \$5.73 per Boe in the same period in 2003.

Operating Expenses

Operating expenses for the year 2004 were \$263 thousand or \$6.52 per Boe compared to \$381 thousand, \$9.54 per Boe, during the same period in 2003. \$90 thousand of operating costs previously expensed were reversed in the fourth quarter. Operating expenses for the year 2003 were increased by start-up costs of a processing plant in Montana and non-payment of operating costs by a joint venture partner.

Netbacks (\$ per Boe)

	Q4 2004	Q4 2003	YTD 2004	YTD 2003
Petroleum and natural gas revenue	42.48	45.60	42.22	44.06
Royalty expense	(5.75)	(7.20)	(6.11)	(5.73)
Operating expense	(1.56)	(9.98)	(6.52)	(9.54)
Net operating income	35.17	28.42	29.59	28.79

General and Administrative Expenses

General and administrative expenses were \$739 thousand or \$18.32 per Boe during the year ended December 31, 2004, an increase of 55% from \$475 thousand or \$11.90 per Boe during 2003. The increased expenditures in 2004 resulted from management, exploration and engineering consulting costs related to the Company's operations in west central Alberta and on its Montana lands. In addition High Plains has experienced higher costs to comply with new financial and reserve reporting requirements. The Company does not capitalize any general and administrative expenditures.

Depletion, Depreciation and Accretion Expense

Depletion, depreciation and accretion expense remained constant at \$411 thousand or \$10.20 per Boe for the year ended December 31, 2004, consistent with \$411 thousand, \$10.30 per Boe in the same period last year. 2003 depletion, depreciation and accretion expense included a \$134 thousand reduction of the carrying value of U.S. processing facilities, reflecting the assignment of no oil and gas reserves to the related oil and gas properties.

Income Taxes

Income tax recovery to December 31, 2004 totalled \$174 thousand, comprised of \$4 thousand current tax expense and \$72 thousand future tax expense related to U.S. operations, offset by \$250 thousand income tax recovery on Canadian operations. The recovery included a \$232 thousand reversal of the valuation allowance on successor pools. In the past, insufficient cash flow was assigned to these properties to make full utilization of the pools likely. As a result of increased oil prices attributed to the successor pools, the valuation allowance was reversed in 2004. The 2003 income tax recovery of \$69 thousand was comprised of current tax expense of

\$20 thousand on the operations of the U.S. subsidiaries and future tax recovery of \$ 89 thousand, \$75 thousand of which applied to operations in Canada.

Estimated Canadian tax pools include:

	(\$ thousands)
Canadian oil and gas property expense	150
Canadian development expense	1,500
Undepreciated capital cost	180
Restricted Canadian exploration expense	1,800
	3,630

Net Income

The Company earned net income of \$281 thousand for the year ended December 31, 2004, down 13% from \$323 thousand net income for the year 2003. The 2004 reduction in earnings was due to increased general and administrative expenses (\$263 thousand) offset by increased net income tax recovery (\$105 thousand), decreased operating expenses (\$118 thousand) and increased foreign exchange gain (\$56 thousand).

Cash flow from operations for the year ended December 31, 2004 decreased 28% to \$473 thousand from \$661 thousand in the same period last year.

Capital Expenditures

During 2004, the Company invested \$1.3 million in capital projects. The projects included the drilling and completing of a new well for liquids-rich natural gas production in the Willesden Green area of Alberta, the recompletion of a well for natural gas production in the Strachan area of Alberta, new drilling for shallow gas in Hill County, Montana, the undertaking of an extensive gravity survey program over the Company's approximate 125,000 net acres in Hill County, Montana and the significant upgrade of the Prairie Dell facility in Toole County, Montana. Comparatively, for 2003, \$477 thousand was invested in the drilling and completion of three Montana wells and the completion of two wells in the Chedderville area of Alberta.

Liquidity and Capital Resources

	December 31, 2004	December 31, 2003
Working capital (deficiency)	(778,733)	5,014

At December 31, 2004, the Company had \$330 thousand of current assets offset by \$1.1 million in current liabilities. During the third quarter, a new well in the Willesden Green area of Alberta was drilled and completed. Partners were cash called for their proportionate share of expenditures, creating a large cash balance while the Company incurred all expenditures, increasing accounts payable. Subsequent to September 30, 2004, the Company paid its suppliers in the normal course of business, utilizing the cash and \$89 thousand of its operating lines.

Two significant Montana projects in the fourth quarter, the Prairie Dell facility upgrade and the Hill County gravity survey, are expected to increase the draw on the Company's operating lines by approximately \$300 thousand when incurred costs are settled.

Credit facilities in place at December 31, 2004 include a revolving operating line of credit authorized to a maximum \$2,500,000 with interest remaining at prime plus 1.25%.

Subsequent to December 31, 2004, the Company completed a private placement. A total of 4,000,000 units were issued at a price of \$0.60 per unit for total gross proceeds of \$2,400,000. Each unit was comprised of one common share and one common share purchase warrant entitling the holder thereof to purchase one common share at a price of \$0.70 per common share expiring two years from date of issuance. Together with the proceeds from this issue, its bank operating lines, and anticipated cash flows from operations, management is of the opinion that the Company has sufficient cash resources available to fund its operations and capital expenditures.

Cash Flow Sensitivities

	Cash Flow (\$)	Per Share Basic
Natural gas price change of \$0.10/Mcf.	17,000	\$0.00
Natural gas sales change of 100 Mcf/day	210,000	\$0.04
Oil price change of US\$1.00 per barrel	5,000	\$0.00
Oil sales change of 30 barrels per day	444,000	\$0.08
Foreign exchange rate of 1% (\$US – Cdn.)	13,000	\$0.00

Cash flow sensitivities are calculated in relation to the Company's annualized revenue and expenses, net of U.S. capital expenditures. The Company has no outstanding hedging contracts.

Related Party Transactions

During 2004, a total of \$238 thousand was paid or accrued to directors and officers of the Company in satisfaction of consulting fees, in accordance with services provided. These amounts are recorded at the exchange amounts agreed to by the related parties. This compares with fees of \$55 thousand during the same period in 2003. The increase in 2004 related primarily to consulting services provided by two officers following the death of the Company's President/CEO and sole employee (\$137 thousand). The \$238 thousand includes \$59 thousand of accrued liabilities related to common share compensation of directors and officers for 2004. The shares are to be issued in 2005.

Share Capital

Securities outstanding as of December 31, 2004 are 5,730,669 common shares. Subsequent to December 31, 2004, 4,000,000 common shares were issued pursuant to a private placement. In addition, 102,785 common shares will be issued which will result in a total of 9,833,454 common shares outstanding.

Of the stock options outstanding as of December 31, 2003, 100,000 options were exercised and 100,000 options were cancelled, leaving a total of 160,000 options outstanding as of December 31, 2004. In the first quarter of 2005, an additional 470,000 options were granted which results in a total of 630,000 stock options outstanding.

Quarterly Financial Information (\$, except per share numbers)

2004	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Petroleum and natural gas revenue	419,537	546,263	396,727	340,427
Cash flow from operations	157,785	194,031	108,490	12,864
Net income	12,075	41,638	57,198	170,571
Net income per share	0.00	0.01	0.01	0.03
Net capital expenditures	261,473	118,163	428,470	482,195

2003	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Petroleum and natural gas revenue	470,866	400,988	421,028	466,969
Cash flow from operations	219,516	106,383	186,967	147,883
Net income	126,471	45,717	89,700	60,865
Net income per share	0.02	0.01	0.02	0.01
Net capital expenditures	174,825	54,613	151,333	96,708

Business Risks

High Plains is engaged in the exploration, development and production of crude oil and natural gas. The oil and gas business is inherently risky and there is no assurance that hydrocarbon reserves will be discovered and economically produced. Operational risks include competition, reservoir performance uncertainties, environmental factors, and regulatory, environment and safety concerns. Financial risks associated with the petroleum industry include fluctuations in commodity prices, interest rates, currency exchange rates and the cost of goods and services.

High Plains contracts highly qualified people, uses sound operating and business practices, and evaluates all potential and existing wells using the latest applicable technology. High Plains complies with government regulations, and environmental and safety policies and standards are adhered to. Asset retirement obligations are recognized upon acquisition, construction, development and/or normal use of the assets. High Plains maintains property and liability insurance coverage. The coverage provides a reasonable amount of protection from risk of loss; however, not all risks are foreseeable or insurable.

Subsequent Events and Corporate Outlook

As a result of significant changes in ownership and senior management early in 2005, the Company is extremely optimistic with respect to its future.

On February 22, 2005, the Company announced a new Board of Directors, management restructuring and private placement financing. The Company confirmed the new Board of Directors and management on March 11, 2005, and, subsequently, on April 22, 2005, the closing of a successful private placement financing.

These initiatives place the Company in a strong position to develop its current asset base and to pursue new oil and gas investments and opportunities. Particularly, the Company expects to direct its resources in the following areas: (i) corporate and/or production acquisitions (ii) evaluation of its large, undeveloped land position in Hill County, Montana (iii) west central Alberta development drilling.

The Company is ambitiously evaluating corporate and production opportunities with the objective to expedite an acquisition. As a result of the recent management restructuring, the Company has been introduced to a number of significant acquisition opportunities. Subject to due diligence and the approval process, it is the ambition of the Company to consummate a transaction as swiftly as possible.

The Company also intends to continue the ambitious exploration and development program of its approximate 125,000 net acres in Hill County, Montana, including a multi-well drilling program. The gravity survey program that was performed in the fourth quarter of 2004 and first quarter of 2005 has rendered extremely encouraging results, which has prompted the company to proceed to the next phase of evaluation. Drilling of the Hill County property could occur as soon as the second half of 2005.

In west central Alberta, where the Company has established production, a number of low to moderate risk drilling opportunities have been identified on or in close proximity to its land holdings. A multi-well drilling program is currently being considered for this area which would add considerable benefit if successful. The Company is also seeking to add to its land holdings in the area.

The entire inventory of properties and operations of the Company will be continuously and thoroughly evaluated to optimize and expedite future growth and success.

High Plains Energy Inc.

Consolidated Financial Statements

December 31, 2004 and 2003

Auditors' Report

To: The Shareholders of
High Plains Energy Inc.

We have audited the consolidated balance sheets of **High Plains Energy Inc.** as at **December 31, 2004 and 2003** and the consolidated statements of income and retained earnings and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2004 and 2003, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Kennedy Mack Slusarchuk Stewart LLP

April 22, 2005

Chartered Accountants

High Plains Energy Inc.

Consolidated Balance Sheets

As at December 31

	2004	2003 (Restated - note-3)
Assets		
Current		
Cash	\$ 35,356	\$ 156,965
Accounts receivable	215,195	288,539
Prepaid expenses	79,695	87,786
	<u>330,246</u>	<u>533,290</u>
Refundable drilling deposit (note 4)	85,640	84,024
Future income taxes (note 9)	700,275	450,249
Property and equipment (note 5)	<u>5,170,271</u>	<u>4,247,158</u>
	<u>\$ 6,286,432</u>	<u>\$ 5,314,721</u>
Liabilities		
Current		
Accounts payable and accrued liabilities	\$ 1,018,004	\$ 510,438
Bank loan (note 6)	88,788	-
Income taxes payable	2,187	17,838
	<u>1,108,979</u>	<u>528,276</u>
Asset retirement obligations (note 7)	632,614	603,384
Future income tax liability (note 9)	<u>396,798</u>	<u>355,435</u>
	<u>2,138,391</u>	<u>1,487,095</u>
Shareholders' Equity		
Share capital (note 8)	1,606,102	1,559,320
Contributed surplus (note 8)	9,641	17,490
Retained earnings	<u>2,532,298</u>	<u>2,250,816</u>
	<u>4,148,041</u>	<u>3,827,626</u>
	<u>\$ 6,286,432</u>	<u>\$ 5,314,721</u>

On behalf of the Board

(signed) "Walter Dawson" Director

(signed) "Ben Anderson" Director

High Plains Energy Inc.

Consolidated Statements of Income and Retained Earnings

For the years ended December 31

	2004	2003 (Restated – note 3)
Revenue		
Petroleum and natural gas	\$ 1,702,954	\$ 1,759,851
Royalties	(246,327)	(228,794)
Other income	9,350	(7,249)
	<u>1,465,977</u>	<u>1,523,808</u>
 Expenses		
Operating	262,629	380,976
General and administrative	738,550	475,438
Depletion and depreciation	384,646	386,551
Accretion	26,496	24,716
Foreign exchange (gain) loss	(53,413)	2,371
	<u>1,358,908</u>	<u>1,270,552</u>
Income before taxes	<u>107,069</u>	<u>253,256</u>
 Income taxes (note 9)		
Current	4,185	19,344
Future	(178,598)	(88,841)
	<u>(174,413)</u>	<u>(69,497)</u>
 Net income	<u>281,482</u>	<u>322,753</u>
 Retained earnings, beginning of year, restated (note 3)	<u>2,250,816</u>	<u>1,928,063</u>
Retained earnings, end of year	<u>\$ 2,532,298</u>	<u>\$ 2,250,816</u>
 Net income per share – basic and diluted (note 8)	<u>\$ 0.05</u>	<u>\$ 0.06</u>

High Plains Energy Inc.
Consolidated Statements of Cash Flows
For the years ended December 31

	2004	2003 (Restated -note3)
Operating		
Net income	\$ 281,482	\$ 322,753
Items not affecting cash:		
Depletion and depreciation	384,646	386,551
Accretion	26,496	24,716
Stock-based compensation expense	3,934	15,570
Unrealized foreign exchange (gain) loss	(44,790)	-
Future income taxes	(178,598)	(88,841)
	473,170	660,749
Changes in non-cash working capital (note 10)	274,320	-
	747,490	660,749
Financing		
Issuance of common shares	35,000	-
Repayment from director	-	17,376
	35,000	17,376
Investing		
Refundable drilling deposit	(1,616)	(2,550)
Expenditures on property and equipment	(1,290,301)	(477,479)
Changes in non-cash working capital (note 10)	387,818	(134,445)
	(904,099)	(614,474)
Increase (decrease) in cash	(121,609)	63,651
Cash, beginning of year	156,965	93,314
Cash, end of year	\$ 35,356	\$ 156,965

High Plains Energy Inc.

Notes to Consolidated Financial Statements

December 31, 2004 and 2003

1. Nature of operations

High Plains Energy Inc. (the "Company") is engaged in the exploration for and production of petroleum and natural gas in Western Canada and the United States. The Company was incorporated under the laws of the Province of Alberta and is listed on the TSX Venture Exchange.

2. Summary of significant accounting policies

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles and include the accounts of the Company and its wholly owned subsidiaries, Griffon Petroleum Inc. and Northern Gas Marketing Inc. Because a precise determination of many assets and liabilities is dependent upon future events, the preparation of periodic financial statements necessarily involves the use of estimates. Accordingly, actual results could differ from those estimates. The financial statements have, in management's opinion, been properly prepared using careful judgment within reasonable limits of materiality and within the framework of the significant accounting policies summarized below:

a) Property and Equipment

(1) Capitalized costs

The Company follows the full cost method of accounting for exploration and development expenditures, wherein all costs related to the exploration for and development of petroleum and natural gas reserves are capitalized in cost centers by country. Capitalized costs include lease acquisition costs, lease rentals on undeveloped properties, geological and geophysical activities, costs of drilling productive and non-productive wells and the cost of petroleum and natural gas equipment.

Proceeds from the disposition of petroleum and natural gas properties are applied to reduce the capitalized costs and no gain or loss is recognized on the disposal of petroleum and natural gas properties unless such disposition would alter the rate of depletion by 20 percent or more.

(2) Depletion and depreciation

Depletion and depreciation of petroleum and natural gas properties are calculated using the unit-of-production method based on total estimated gross proven petroleum and natural gas reserves, as determined by independent engineers. Relative volumes of petroleum and natural gas reserves and production are converted to a common measure on the basis of their relative energy content of six thousand cubic feet of natural gas to one barrel of oil. Other equipment is provided for on the straight-line basis at 20% per annum.

(3) Impairment test

In applying the full cost method, the Company calculates a ceiling test for each cost center whereby the carrying value of property and equipment is compared to the sum of the undiscounted cash flows expected to result from the future production of proved reserves and the sale of unproved properties. Cash flows are based on third party quoted forward prices, adjusted for transportation and quality. Should the ceiling test result in an excess of carrying value, the Company would then measure the amount of impairment for the cost center by comparing the carrying amounts of property and equipment to an amount equal to the estimated net present value of future cash flows from proved plus probable reserves and the sale of unproved properties. A risk-free interest rate is used to arrive at the net present value of the future cash flows. Any excess carrying value would be recorded as a permanent impairment.

High Plains Energy Inc.

Notes to Consolidated Financial Statements

December 31, 2004 and 2003

b) Asset retirement obligations

The Company recognizes the fair value of a liability for any asset retirement obligation in the period in which it is incurred and records a corresponding increase in the carrying value of the related long-lived asset. The fair value is determined through a review of engineering studies, industry guidelines, and management's estimate on a site by site basis. The liability is subsequently adjusted for the passage of time, and is recognized as an accretion expense in the statement of income. The liability is also adjusted due to revisions in either the timing or the amount of the original estimated cash flows associated with the liability. The increase in the carrying value of the asset is amortized using the unit of production method based on estimated gross proven reserves as determined by independent engineers. Actual costs incurred upon settlement of the asset retirement obligations are charged against the asset retirement obligation to the extent of the liability recorded. Any difference between the actual costs incurred upon settlement of the asset retirement obligations and the recorded liability is recognized as a gain or loss in the Company's statement of operations in the period in which the settlement occurs.

c) Joint operations

A portion of the Company's exploration, development and production activities are conducted jointly with others and, accordingly, these financial statements reflect only the Company's proportionate interest in such activities.

d) Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The amounts recorded for depletion and depreciation of property and equipment and the provision for asset retirement costs and the ceiling test are based on estimates of gross proven reserves, production rates, oil and gas prices, future costs and other relevant assumptions. Stock-based compensation fair value calculations are based on estimates of dividend yield, forfeiture rate, volatility and risk-free rate. Estimates are reviewed regularly and changes in such estimates in future years could be significant. As adjustments become necessary, they are reported in earnings in the periods in which they become known.

e) Revenue recognition

Petroleum and natural gas revenues are recognized when title passes from the Corporation to its customers.

f) Cash and cash equivalents

Cash and cash equivalents include bank accounts, an operating line, and term deposits with maturities of less than three months.

g) Future income taxes

The Company follows the liability method of accounting for income taxes. Under this method future income tax assets and liabilities are determined based on differences between financial reporting and income tax bases of assets and liabilities, and are measured using substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse. The effect on future tax assets and liabilities of a change in tax rates is recognized in net income in the period in which the change is substantively enacted. To the extent that the Company does not consider it to be more likely than not that a future tax asset will be recovered, it provides a valuation allowance against the excess.

High Plains Energy Inc.

Notes to Consolidated Financial Statements

December 31, 2004 and 2003

h) Foreign exchange

Monetary assets and liabilities of integrated foreign operations are translated into Canadian dollars at the rate of exchange in effect at the balance sheet date. Other assets, liabilities, and items affecting earnings are translated into Canadian dollars at rates of exchange in effect at the date of the transaction, except for depletion and amortization. Depletion and amortization are translated at the same rate as the related assets. Gains or losses arising from foreign currency translation are included in the determination of income.

i) Stock options

Under the Company's stock option plan, options to purchase common shares are granted to directors, officers and employees at current market prices. Options granted by the Company since January 1, 2003 are accounted for in accordance with the fair-value method of accounting for stock-based compensation, and as such the cost of the option is charged to earnings with an offsetting amount recorded to contributed surplus, based on an estimate of the fair value using a Black-Scholes option-pricing model. No compensation expense has been recorded on options issued in 2002 (see note 8).

j) Per share amounts

The treasury stock method of calculating per share amounts is used whereby any proceeds from the exercise of stock options or other dilutive instruments are assumed to be used to purchase common shares at the average market price during the period.

3. Change in accounting policy

Effective January 1, 2004, the Company adopted the recommendations of the Canadian Institute of Chartered Accountants on accounting for asset retirement obligations for related long-term assets as a liability. Retirement costs equal to the present value of the retirement obligation are capitalized as part of the cost of property and equipment and amortized to expense through depletion over the life of the asset. The change in the liability due to the passage of time is measured by applying an interest method of allocation to the opening liability and is recognized as an increase in the carrying value of the liability and an expense. The expense is recorded as an operating item in the income statement, not as a component of interest expense. A change in the liability resulting from revisions to either the timing or the amount of the original estimate of undiscounted cash flows is recognized as an increase or decrease in the carrying amount of the liability, with an offsetting increase or decrease in the carrying amount of the associated asset. This standard was adopted retroactively January 1, 2004, and prior period comparative balances were restated.

The adoption of this standard had the following effects on the Company's consolidated financial statements:

	Previously reported \$	Adjustment \$	Restated \$
As at December 31, 2003			
Property and equipment	3,847,418	399,740	4,247,158
Asset retirement obligations	193,177	410,207	603,384
Future income tax asset	425,000	25,249	450,249
Future income tax liability	361,000	(5,565)	355,435
Retained earnings	2,230,469	20,347	2,250,816
For the year ended December 31, 2003			
Depletion and depreciation	355,017	31,534	386,551
Site restoration provision	30,750	(30,750)	-
Accretion	-	24,716	24,716
Future tax provision	(58,300)	(30,541)	(88,841)
Retained earnings, beginning of year	1,912,757	15,306	1,928,063

High Plains Energy Inc.

Notes to Consolidated Financial Statements

December 31, 2004 and 2003

4. Refundable drilling deposit

The refundable drilling deposit is with the State of Montana and bears interest at 1.87% (2003 - 2.00%)

5. Property and equipment

		December 31, 2004		
		Accumulated depletion and depreciation		
	Cost			Net
Petroleum and natural gas properties	\$ 7,163,052	\$ 2,002,294	\$	5,160,758
Office equipment	31,992	22,479		9,513
	<u>\$ 7,195,044</u>	<u>\$ 2,024,773</u>	<u>\$</u>	<u>5,170,271</u>

		December 31, 2003 Restated - note 3		
		Accumulated depletion and depreciation		
	Cost			Net
Petroleum and natural gas properties	\$ 5,866,691	\$ 1,628,646	\$	4,238,045
Office equipment	29,492	20,379		9,113
	<u>\$ 5,896,183</u>	<u>\$ 1,649,025</u>	<u>\$</u>	<u>4,247,158</u>

The Company did not capitalize any general and administrative costs during 2004 and 2003. No unproved properties were excluded from the depletion base in 2004 and 2003.

The Company applied the ceiling test to its capitalized assets at December 31, 2004 and determined that there was no impairment of costs requiring a write-down. For the purposes of the December 31, 2004 impairment test of property and equipment, the following prices based on price forecasts for the reference price of oil at Edmonton and gas postings at AECO, adjusted for quality and transportation costs, were used:

	2005	2006	2007	2008	2009	Thereafter
Natural gas (\$/mcf)						
Canada	6.75	6.35	5.94	5.59	-	-
United States	6.71	6.50	6.24	5.98	5.70	+ 2.0%
Crude oil (\$/bbl)						
Canada	46.08	44.06	41.72	38.67	36.55	+ 1.8%

6. Bank loan

The Company has a revolving operating line of credit of \$2,500,000 with interest at prime plus 1.25% of which \$88,788 was drawn at December 31, 2004 (2003 - \$ nil).

The loan facilities are secured by an assignment of accounts receivable and a \$5,000,000 debenture with a floating charge over all assets of the Company with a Negative Pledge and Undertaking to provide fixed charges on the Company's major producing petroleum properties at the request of the bank.

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7. Asset retirement obligations

The Company retroactively adopted the new standard for accounting for asset retirement obligations on January 1, 2004 and accordingly the previous year's financial statements have been restated as in Note 3.

The following table presents the reconciliation of the carrying amount of the obligation associated with the retirement of the Company's property and equipment.

	December 31 2004	December 31 2003
Asset retirement obligations, beginning of year	\$ 603,384	\$ 578,668
Liabilities incurred	18,777	-
Accretion	26,496	24,716
Liabilities settled	-	-
Effect of foreign exchange conversion	(16,043)	-
Asset retirement obligations, end of year	\$ 632,614	\$ 603,384

The following significant assumptions were used to estimate the asset retirement obligation:

	December 31 2004	December 31 2003
Undiscounted cash flows	\$ 980,500	\$ 951,800
Risk-free discount rate, adjusted for inflation	4.25%	4.25%
Expected timing of cash flows	4 – 14.5 years	5 – 15 years

8. Share capital

a) Authorized

Unlimited number of Common voting shares

Unlimited number of First Preferred shares issuable in series

Unlimited number of Second Preferred shares issuable in series

b) Issued

	Number of Shares	Amount
Common shares		
Balance – December 31, 2002 and 2003	5,630,669	\$ 1,559,320
Stock options exercised – cash proceeds	100,000	35,000
Stock options exercised – contributed surplus	-	11,782
Balance – December 31, 2004	5,730,669	1,606,102
Contributed Surplus		
Balance – December 31, 2002		\$ 1,920
Stock-based compensation		15,570
Balance – December 31, 2003		\$ 17,490
Stock-based compensation		10,535
Cancellation of stock options		(6,602)
Exercise of stock options		(11,782)
Balance – December 31, 2004		\$ 9,641

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c) Stock options

The Corporation has established a stock option plan for its directors, officers and key employees. Pursuant to this plan, the Corporation is authorized to reserve for issuance up to 10% of its common shares outstanding from time to time. Options expire five years from the date of grant and vest over periods as determined by the Board of Directors at the time of grant. Currently, the Company's policy is to issue options that vest equally over a three year period from the date of grant.

The fair value of the stock options was estimated for 2004 and 2003 using the Black-Scholes option pricing model with the following assumptions: zero dividend yield, no forfeiture rate, expected volatility of 96%, risk-free rate of 4.25% and expected life of five years. The Corporation has recognized the estimated value of \$3.934 as stock-based compensation expense related to options for the year ended December 31, 2004. The weighted average grant date fair value was \$0.15 per option in both years.

The following is a continuity of stock options outstanding for which shares have been reserved:

	December 31, 2004		December 31, 2003	
	Options	Weighted – Average Exercise Price \$	Options	Weighted – Average Exercise Price \$
Opening	360,000	0.32	160,000	0.33
Granted	-	-	250,000	0.35
Cancelled	(100,000)	0.35	(50,000)	(0.40)
Exercised	(100,000)	0.35	-	-
Closing	160,000	0.28	360,000	0.32

The following tables summarize information about stock options outstanding as at December 31, 2004:

Exercise Price \$	Number Outstanding	Weighted Average Remaining Contractual Life (years)	Number Exercisable	Weighted Average Exercise Price \$
0.20	50,000	0.2	50,000	0.20
0.30	60,000	1.2	60,000	0.30
0.35	50,000	3.5	50,000	0.35
	160,000	1.6	160,000	0.28

d) Per share amounts

Per common share calculations are based on the following weighted average number of common shares outstanding during the period:

	Year ended December 31	
	2004	2003
Basic	5,666,188	5,630,669
Diluted	5,738,688	5,662,041

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9. Income taxes

Income tax expense differs from what would be expected by applying the effective income tax rate of 39.62% (2003 - 40.62%) to Canadian income and 36.30% (2003 - 36.30%) to United States income. The difference results from the following:

	2004			2003
	Canada	United States	Total	Total
				(Restated – note 3)
Expected income tax provision	\$ (66,642)	\$ 99,924	\$ 33,282	\$ 101,845
Increase (decrease) income tax provision:				
Change in tax rates	26,253		26,253	39,840
Reduction due to graduated rates		(11,708)	(11,708)	(11,258)
Statutory depletion		(13,187)	(13,187)	(51,193)
Decrease in valuation allowance	(232,303)		(232,303)	(117,409)
Asset retirement obligation				(30,541)
Other	22,666	584	23,250	(781)
	<u>\$ (250,026)</u>	<u>\$ 75,613</u>	<u>\$ (174,413)</u>	<u>\$ (69,497)</u>

The significant components of the Company's future income tax asset related to Canadian operations are as follows:

	2004	2003
		(Restated – note 3)
Tax basis of property and equipment in excess of carrying value	\$ 549,444	\$ 623,000
Asset retirement obligation	147,006	53,249
Share issue costs	3,825	6,000
	<u>700,275</u>	<u>682,249</u>
Valuation allowance	-	(232,000)
	<u>\$ 700,275</u>	<u>\$ 450,249</u>

The valuation allowance relates to successor oil and gas tax pools which were not expected to be fully utilized based on previous estimates. As a result of increased reserves attributed to these pools, the valuation allowance has been reversed in 2004.

The significant components of the Company's future income tax liability related to United States operations are as follows:

	2004	2003
		(Restated – note 3)
Carrying value of property and equipment in excess of tax basis	\$ 425,240	\$ 392,000
Asset retirement obligation	(28,442)	(36,565)
	<u>\$ 396,798</u>	<u>\$ 355,435</u>

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10. Changes in non-cash working capital

	Year ended December 31	
	2004	2003
Accounts receivable	\$ 73,344	\$ (74,915)
Prepaid expenses	8,091	(87,786)
Accounts payable and accrued liabilities	596,354	10,418
Income taxes payable	(15,651)	17,838
	<u>\$ 662,138</u>	<u>\$ (134,445)</u>

The change in non-cash working capital has been allocated to the following activities:

	Year ended December 31	
	2004	2003
Operating	\$ 274,320	\$ -
Investing	387,818	(134,445)
	<u>\$ 662,138</u>	<u>\$ (134,445)</u>

11. Related parties

During the year ended December 31, 2004, the Company was charged \$238,235 (2003 – \$55,187) by directors and officers for administrative and consulting services. These amounts are recorded at the exchange amounts agreed to by the related parties.

12. Segmented disclosure

	Year ended December 31, 2004		
	Canada	United States	Total
Petroleum and natural gas revenue	\$ 727,737	\$ 975,217	\$ 1,702,954
Royalties	(105,342)	(140,985)	(246,327)
Other income	6,912	2,438	9,350
Operating and general and administrative expense	(596,487)	(404,692)	(1,001,179)
Depletion, depreciation and accretion	(201,023)	(210,119)	(411,142)
Foreign exchange gain	-	53,413	53,413
Income tax (expense) recovery	250,026	(75,613)	174,413
Net income (loss)	81,823	199,659	281,482
Earnings (loss) per share:			
Basic and diluted	0.01	0.04	0.05
Total assets	3,092,815	3,193,617	6,286,432
Long term liabilities	420,016	609,396	1,029,412
Expenditures on petroleum and natural gas properties and equipment	809,014	481,287	1,290,301

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	Year ended December 31, 2003		
	(Restated – note 3)		
	Canada	United States	Total
Petroleum and natural gas revenue	\$ 535,067	\$ 1,224,784	\$ 1,759,851
Royalties	(54,232)	(174,562)	(228,794)
Other income	1,119	(8,368)	(7,249)
Operating and general and administrative expense	(404,229)	(452,185)	(856,414)
Depletion, depreciation and accretion	(62,214)	(349,053)	(411,267)
Foreign exchange loss	-	(2,871)	(2,871)
Income tax (expense) recovery	99,976	(30,479)	69,497
Net income (loss)	115,487	207,266	322,753
Earnings (loss) per share:			
Basic and diluted	0.02	0.04	0.06
Total assets	3,079,212	2,235,508	5,314,721
Long term liabilities	396,990	561,829	958,819
Expenditures on petroleum and natural gas properties and equipment	133,544	343,935	477,479

13. Financial instruments

a) Fair values of financial assets and liabilities

Financial instruments of the Company consist mainly of cash, accounts receivable, deposits, bank loan and accounts payable and accrued liabilities. As at December 31, 2004 and 2003 there are no significant differences between the carrying amounts reported on the balance sheet and their estimated fair values.

b) Credit risk

The majority of the Company's accounts receivable are in respect of oil and natural gas operations. The Company generally extends unsecured credit to these customers, and therefore, the collection of accounts receivables may be affected by changes in economic or other conditions and may accordingly impact the Company's overall credit risk. Management believes the risk is mitigated by the size and reputation of the companies to which they extend credit.

c) Exchange rate risk

The Company is subject to exchange rate risk as a portion of its working capital is denominated in U.S. dollars.

d) Interest rate risk

The Company is subject to a floating interest rate on its credit facilities.

e) Commodity price risk

The nature of the Company's operations results in exposure to fluctuation in commodity prices.

At December 31, 2004 the Company has no forward contracts outstanding or any derivative instruments related to exchange rates, interest rates or commodity prices.

14. Comparative figures

The financial statements have been reclassified, where applicable, to conform to the presentation used in the current year. The changes do not affect prior years' earnings.

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15. Subsequent events

- (a) During the period between January 11 and February 9, 2005, Perfco Investments Ltd. acquired 930,500 common shares of the Company at an average price of \$0.60 per share, representing approximately 16.24% of the outstanding common shares at December 31, 2004. Four of the five board members resigned in their capacities as directors and officers of the Company and four new board members were appointed.
- (b) In the first quarter of 2005, 470,000 stock options were granted by the Company to directors and officers at exercise prices of \$0.60 and \$0.70 per share. The options vest one third per year on the anniversary date of grant and expire five years from the date of grant. In addition, the board of directors approved the issuance of 102,785 common shares at a deemed issue price of \$0.70 per share to departing directors and officers in consideration of 2004 and 2005 past service. At December 31, 2004, \$60,000 of this liability is included in general and administrative expense for services provided in 2004.
- (c) On April 14, 2005, the Company closed a private placement of 4,000,000 units at an issue price of \$0.60 per unit for gross proceeds of \$2,400,000. Each unit consists of one common share and one common share purchase warrant which allows for the purchase of one common share at a price of \$0.70 per common share for a period of two years.

